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In The

Supreme Court of the United States

October Term — 1968

No. 783

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D. C. TRANSIT SYSTEM, INC.,

Petitioner,

v.

RICHARD A. WILLIAMS, ALFRED S. TRASK, DEMOCRATIC CENTRAL COMMITTEE OF THE DISTRICT OF COLUMBIA, LEONARD N. BEBCHICK, DANIEL W. GOTTLIEB and WASHINGTON METROPOLITAN AREA TRANSIT COMMISSION,

Respondents.

On Petition for a Writ of Certiorari to The United States Court of Appeals for The District of Columbia Circuit

BRIEF FOR RESPONDENTS IN OPPOSITION

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BRIEF FOR RESPONDENTS IN OPPOSITION

QUESTION PRESENTED

The question is whether the United States Court of Appeals for the District of Columbia Circuit having jurisdiction under the Washington Metropolitan Area Transit

Compact ("Compact") to review orders of the Washington Metropolitan Area Transit Commission ("Commission") exceeded its powers as a court of review when (1) it set aside two rate-making orders of the Commission (then superseded by subsequent rate-making orders) on the grounds that the orders were unsupported by necessary findings and reflected arbitrariness in failing to consider and apply statutory standards previously enunciated by the Court; and (2) as an incident to such ~~order~~ action and in the exercise of judicial discretion, it ordered partial restitution of amounts received by the utility under the unlawful orders set aside.

STATEMENT

On April 8, 1965, the court below remanded to the Commission for further consideration its Order 245 which had authorized a 1963 increase in the fares charged by D.C. Transit System, Inc. ("Transit"). *D.C. Transit System, Inc. v. Washington Metropolitan Area Transit Commission,* 350 F.2d 753 (D.C. Cir., *en banc,* 1965) hereinafter "Transit I").[1] The court found that the Commission had described its deliberations and conclusions on the fundamental question of fair return "in terms of stock generalizations which serve only to frustrate, rather than illuminate, judicial review." (Appendix, A-7). As the court was confronted with "the Commission's failure to provide us an adequate basis for knowing why it did and what it did", it directed the Commission upon remand "to determine the margin of return over and above operating expenses that Transit should be allowed." (Appendix, A-10). Neither the Commission nor Transit sought to obtain certiorari.

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[1] For convenience the relevant portions of the Court of Appeals opinion in Transit I are set out in the Appendix ("Appendix") at the close of this brief. These portions are also found at 350 F.2d 777-781.

The Commission had set Transit's return by a purported application of the "operating ratio" method of ratemaking an approach prescribed by the Compact (Page A-2 of Petitioner's Appendix, hereinafter cited "Petit. App.") and whose proper application has been approved by the court below both prior and subsequent to this litigation.[2] The court undertook to disabuse the Commission of the belief that such a ratemaking method might properly be applied simply by plucking any particular operating ratio figure from the air. The court took great pains to enlighten the Commission as to the lawful predicate for a proper application of the operating ratio standard in setting rates and as to the various areas of factual inquiry required to support necessary findings. This brief will be foreshortened and the Court's comprehension of the Petition facilitated by a recitation here of what the Court of Appeals said in 1965:

> "We do not quarrel with the Commission's conclusion that Congress intended that the operating ratio method should be the primary test of the reasonableness of Transit's fares. But the language that appears in its order strongly suggests that it misunderstood what that test entails. In *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591,602 (1944), the Supreme Court enunciated what is now a fundamental principle of rate regulation: "Under the statutory standard of 'just and reasonable'

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[2] *Bebchick v. Public Utilities Commission*, 318 F.2d 187 (D.C. Cir., 1963), *cert. den'd.*, 373 U. S. 913 (1963); *Payne, et. al v. Washington Metropolitan Area Transit Commission* and *D.C. Transit System, Inc. v. Washington Metropolitan Area Transit Commission (Consolidated)*, Nos. 20,988 and 21,029, ___ F.2d ___ (D.C. Cir., October 8, 1968).

it is the result reached not the method employed which is controlling." (Emphasis added.) The Court went on to point out that, in balancing investor and consumer interests, it is essential to consider the capital costs of the enterprise. 320 U.S. at 603. Here, unlike the *Hope* case, Congress has specified what method of rate making the Commission should employ, but in so doing it did not relieve the Commission of the necessity of making the kind of inquiry that must be made if the statutory standard is to be complied with. A "just and reasonable" rate is one that assures that all the enterprise's legitimate expenses will be met, and that enables it to cover interest on its debt, pay dividends sufficient to continue to attract investors, and retain a sufficient surplus to permit it to finance down payments on new equipment and generally to provide both the form and substance of financial strength and stability. A rate fixed without particularized reference to these needs does not satisfy any standard of rate making of which we are aware, including that of return on operating expenses. The operating ratio method does not make such an inquiry irrelevant; indeed, it was in part the failure of rates established by the rate base method to cover the capital costs of most motor carriers that led to its adoption. ***

We know from this figure of 95.13 only that the legitimate operating expenses found by the Commission – and we accept that legitimacy in this case – account

for all but 4.87 per cent of the total revenues expected to be realized from the approved fare structure. We need to know more than we have been told about why the Commission thought this was the appropriate margin. The fixing of that margin is not in truth a process so greatly different from what is done in determining rate of return in traditional rate-base rate-making. There also the gross revenues allowed are to cover legitimate operating expenses in the first instance – and something more. That something more is the sum of money needed to attract the capital, both debt and equity, required to insure financial stability and the resulting capacity of the utility to render the service upon which the public depends. To determine that sum entails inquiries and findings–judgmental as the latter may often be because rate-makers must be prophets of the future as well as historians of the past–into such things as the capital programs in prospect, what such programs entail in terms of down-payments as well as financing, the cost of borrowing money, working capital needs, the desirable ratio of debt to equity, the incentives required by a stockholder to keep his money in the business and the dividends and growth rates requisite to supply these incentives, the opportunities in these respects provided in comparable businesses, and the related matters which must be prayerfully explored by the conscientious regulator before he can begin to say why he fixed upon 4.87 rather than 6.5 or 3.2." (Appendix, A-5 *et. seq.*).

Upon remand the Commission without further proceedings issued a supplementary order (No. 563) affirming its earlier determination. On the same date it issued Order No. 564 arising out of a subsequent rate proceeding wherein the Commission increased Transit's allowable return. The company was permitted to realize the increased return by a withdrawal from a court-ordered reserve[3] in lieu of an increase in fares.

Your respondents sought review of both Orders and the appeals were consolidated. The Court of Appeals on October 8, 1968, sitting *en banc* and acting unanimously set aside the Orders and directed that partial restitution be made in respect of fares collected under Orders 245 and 563 and amounts withdrawn from the court-ordered reserve under Order 564. The court below rejected not only the level of fair return established by the Commission in both proceedings, but also a variety of expense allowances and accounting adjustments. The implementation of the decree of restitution will require a variety of factual determinations to be made by the Commission on remand. Petitioner here seeks certiorari only in respect of the court's action in setting aside the Commission's determination in Order Nos. 245, 563 and 564 as to the level of fair return which Transit should be permitted to earn and in awarding restitution.

In passing upon a question of fair return in its decision for which certiorari is sought, the court below stated:

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[3] The reserve was established as a means of providing restitution to transit users for previously authorized unlawful fare increases. *Bebchick v. Public Utilities Commission*, 318 F.2d 187, 203-204 (D.C. Cir. *en banc*, 1963), *cert den'd.*, 373 U.S. 913 (1963).

> "The case now before us, however, is quite different. The Commission, once again, does not advance a rational basis for its determination of rate of return – despite the opportunity afforded it to do so, after we had enunciated the applicable principles and emphasized the need for findings. Moreover, it now appears affirmatively that at no time in this proceeding has the Commission made the investigations and the resolutions essential to a legitimate exercise of its authority to prescribe just and reasonable fares. Since we cannot escape the conclusion that the Commission's approval of the fare increase was based upon a mistaken view of its responsibilities in setting rates under the operating ratio method, we hold that Order Nos. 245 and 563 must be set aside." [Footnotes Omitted] (Petit. App., B-26, B-27).

In a similar vein, the court elsewhere in its opinion observed that despite the explicit guidelines which it earlier had set forth, it searched the Orders in vain to find any of the vital and essential findings or any manifestation of inquiry into any of the pertinent considerations called for. Moreover, it saw little in the way of particularized reference to matters discussed in the remand opinion. (Petit. App., B-7, B-24, B-82).

The court below then determined in an exhaustive analysis of precedent that no further remand was warranted particularly in view of the fact that the rate orders in question had been superseded and the Commission did not possess retroactive ratemaking powers. (Petit. App., B-28 through B-31). Finally, the court, consistent with earlier practice and in accordance with a detailed analysis of legal precedent, awarded partial

restitution of certain amounts received by Transit under the Orders set aside. (Petit. App., B-32 through B-41).

ARGUMENT

A. Introduction

1. The best response to the Petition is the opinion of the court below. This is not only because the opinion is exceptional in its length, detail and extensive analysis of every issue presented, but essentially because the petitioner's characterization of what the court did bears little relationship to what in fact its opinion says. We respectfully direct the attention of this Court to the applicable portions of the opinion below. (Petit. App., B-1 through B-41; B-82 through B-101).

2. The opinion below is that of an *en banc* Court of Appeals and represents the *unanimous* determination of the sitting judges. It is the third such *en banc* review determination of agency action in the setting of fares charged by Transit.[4] The issues involved are routine and the court's action is simply another instance of setting aside arbitrary agency action for want of adequate findings and failure to adhere to statutory standards. Petitioner asks the Court to become involved in regulatory aspects of bus transportation in the District of Columbia under a Compact limited in application to the Washington Metropolitan area and effective upon only a few bus companies of which Transit is by far the largest. This is precisely the type of local D.C. subject matter with which this Court repeatedly has declined to become involved. *Fisher v. U.S.*, 328 U.S. 463, 476 (1946); *District of Columbia v. Pace*, 320 U.S. 698, 702 (1944); *Busby v. Electric Utilities Union*, 323 U.S. 72, 74-75 (1944).

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[4] *Bebchick v. Public Utilities Commission*, cited *supra*, Ftn. 2; *Transit I*, cited *supra*, p. 2.

B. The Issue of Fair Return

1. Petitioner suggests that the decision of the court below as to the legal requisites for a proper application of the operating ratio standard of ratemaking possesses national importance and implication. The fact is that to our best knowledge no Federal statute, including those applicable to the Interstate Commerce Commission, specifies as does the Compact the employment of an operating ratio method of ratemaking. Moreover, the definitive views of the Court of Appeals on this subject (Transit I, cited, *supra,* p. 2) have been in the public domain for almost four years and we are unaware of a single instance in which these views in any way have impeded or adversely affected the effective discharge of ratemaking duties by any regulatory agency. Given the considerable time which has elapsed since the decision in Transit I, we would have expected that Transit would have been able to provide some factual basis to support its unwarranted speculations.

2. As far as concerns the operating ratio standard, we understand the thrust of Transit's Petition to be that the court below erroneously rejected such standard. The court, of course, did no such thing. It merely reiterated and relied upon long-standing precedents – that the establishment of just and reasonable rates by whatever method must result from a determination based upon adequate findings and substantial evidence that the rate is one that covers a utility's reasonable expenses, its debt and capital costs, and yields a sufficient margin to provide financial strength and stability and is commensurate with the returns of other companies of similar risk so as to enable it to attract investors. As indicated in the Statement, the court below has approved establishment of rates by the operating ratio method when it has been properly applied (*supra,* Ftn. 2).

3. Transit errs in taking the court below to task for purportedly announcing for the first time a new and different standard – the cost of capital. But as the court

made clear (Petit. App., B-12 through B-19) and as it did in Transit I (Statement *supra,* pp. 4-5), the cost of capital is simply a relevant factor which the Commission must pass upon or provide a rational basis for rejecting. As the court stated, "It suffices to again point out that if a 'cost of capital approach' is to be dismissed as 'inappropriate' or spurned as 'not wholly applicable', it is incumbent upon the Commission to say why and to set forth for the record, through analysis and findings, the alternate method it employed to determine fair return." (Petit. App., B-88 through B-89).

4. Although not raised in any manner either before the Commission or the court below, Petitioner contends that the court erred in not approving any level of fair return established by the Commission which yields less than 6½% of gross operating revenues. That issue was fully briefed and decided adversely to Transit in Transit I (*D.C. Transit System, Inc. v. WMATC,* cited *supra,* p. 2, 350 F.2d at 758-766), a determination from which Transit did not seek the review of this Court. Petitioner's reliance upon some incidental language of this Court appearing in *Universal Interpretive Shuttle Co. v. Washington Metropolitan Area Transit Commission* (No. 19, Slip Op. p. 4, November 25, 1968) is of no avail. The question of whether the Commission is compelled by law to grant Transit any return it seeks which amounts to less than 6½% of gross operating revenues was not presented or considered in any form in that litigation.

C. The Relief Granted.

1. The balance of Transit's Petition deals with the relief granted by the court below – the setting aside of challenged Orders and the partial award of restitution. The court was well within its powers in setting aside orders which lacked adequate findings and represented a misapplication of statutory standards previously announced. The only durable protection which consumers have against

unlawful ratemaking is that the utility sustain its burden of proof in seeking higher fares and that the agency formulate an order which meets lawful standards, is rational, and is supported by adequate findings based on substantial evidence. The interest of consumers is sacrificed and the vitality of the regulatory process dissipated if rate decisions are ping-ponged back and forth between court and commission until a commission finally is able to discover language sufficient to muster judicial scrutiny.[5] The expense, delay and unsatisfactory result to consumers of such procedures would result in aborting the few consumer challenges to regulatory rulings which now are taken.

The court below, however, decided against remand on narrower ground founded on established precedent which it painstakingly reviewed (Petit. App., B-28 through B-36). As all of the Orders in question had been superseded by subsequent Commission determinations approving new schedules of fares and since the court believed that the Commission lacked the power to enter a new rate order applicable retroactively *nunc pro tunc*, it determined that a remand for further consideration was not called for. Petitioner's challenge to this ruling is represented by a one sentence assertion that the court's "reasoning is completely fallacious". (Petition p. 22). A more compelling analysis is required to justify grant of certiorari.

2. The balance of the Petition in effect challenges the authority of the court below to order restitution in

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[5] Here, no remedy has yet been implemented for Petitioner's unlawful fare increase which occured in 1963. In cases where a utility has overcharged its users there is a public interest in effecting the remedial decree at the earliest feasible time. See *Federal Power Comm. v. Tennessee Gas Transmission Co.*, 371 U.S. 145, 154-155 (1962).

the exercise of its judicial function. The court in the circumstances presented felt restitution warranted because to permit Transit to retain the increased fares would be to give legal effect to the Commission's invalid orders (Petit. App., B-32 through B-41, B-95 through B-97).

Upon a detailed analysis of precedent,[6] the court found the award of restitution in such circumstances to be not a matter of right but a determination *ex gratia* resting in the exercise of the sound discretion by the court. Rather than awarding restitution for the full amount collected under the unlawful Orders as it had done in an earlier decision involving Transit,[7] the court directed that restitution be made only for the difference between the amounts received by Transit under the unlawful orders and the amounts of fair return which your respondents and their expert witnesses contended were fair and reasonable. In so acting, the court gave considerable weight to a subsequent Commission rate Order sustained by the court on review, which authorized a fair return to Transit quite close to that recommended by respondents in the instant litigation (Petit. App., B-41 and B-96 through B-97). The court narrowly circumscribed its action with the express caveat that it was not deciding whether in the absence of such a subsequent Commission determination, the course it decided to take otherwise would be open to it.

Contrary to Transit's assertions, the court did not undertake to determine the just and reasonable fares which Transit should be permitted to charge or to sanction for any ratemaking purposes any particular level of fare return which it should be permitted to earn.

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[6] See cases collected in Ftn. 97 of the opinion (Petit. App., B-33); also see *Capital Transit Co. v. Public Utilities Commission*, 213 F.2d 176, 194-96 (D.C. Cir., 1954), *cert. den'd.*, 348 U.S. 816 (1954).

[7] *Bebchick v. Public Utilities Commission*, cited *supra*, Ftn. 2.

It correctly noted:

> "Our role as a reviewing court is not to make an independent determination as to whether fares fixed by the Commission are just and reasonable, but rather to ensure that the Commission, in exercising its rate-making power, has acted rationally and lawfully. (Petit. App., B-33).

The court in the exercise of the judicial function was "confronted with the necessity of formulating the criteria by which the amount of restitution is to be measured." (Petit. App., B-35). In establishing the appropriate criteria of restitution, the court was acting well within the ambit of its equity powers and was not undertaking to exercise the ratemaking power bestowed by statute upon the Commission. It merits emphasizing that – despite the claims made in the Petition – the court at no time attempted to determine what just and reasonable fares Transit should be permitted to charge or what amount of fair return it should be allowed to receive under schedules of fares lawfully established by the Commission.

CONCLUSION

For the foregoing reasons, the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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DATED: January 17, 1969

APPENDIX

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 17,953

D. C. TRANSIT SYSTEM, INC., PETITIONER,

v.

WASHINGTON METROPOLITAN AREA TRANSIT COMMISSION, RESPONDENT, ALFRED S. TRASK AND RICHARD A. WILLIAMS, UNITED STATES OF AMERICA, INTERVENORS.

No. 17,954

RICHARD A. WILLIAMS AND ALFRED S. TRASK, PETITIONERS,

v.

WASHINGTON METROPOLITAN AREA TRANSIT COMMISSION

AND

D. C. TRANSIT SYSTEM, INC., RESPONDENTS,

UNITED STATES OF AMERICA, INTERVENOR.

On Petitions to Review an Order of the Washington Metropolitan Area Transit Commission

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Decided April 8, 1965

Mr. Harvey M. Spear, with whom *Messrs. John R. Sims, Jr., Edmund L. Jones* and *John J. Ross* were on the brief, for D. C. Transit System, Inc., petitioner in No. 17,953 and respondent in No. 17,954.

Mr. Leonard N. Bebchick for Williams and Trask, petitioners in No. 17,954 and intervenors in No. 17,953. *Mr. Harold Leventhal* also entered an appearance for Williams and Trask.

Mr. Russell W. Cunningham for respondent Washington Metropolitan Area Transit Commission.

Mr. I. Daniel Stewart, Jr., Attorney, Department of Justice, of the bar of the Supreme Court of Utah, *pro hac vice,* by special leave of court, with whom *Assistant Attorney General William H. Orrick, Jr.,* and *Mr. Lionel Kestenbaum,* Attorney, Department of Justice, were on the brief, for intervenor United States of America.

Before BAZELON, *Chief Judge,* WILBUR K. MILLER,* FAHY, WASHINGTON, DANAHER, BASTIAN,* BURGER, WRIGHT, and McGOWAN, *Circuit Judges,* sitting *en banc.*

McGOWAN, *Circuit Judge,* with whom BAZELON, *Chief Judge,* FAHY, WASHINGTON, DANAHER, BASTIAN,* BURGER, and WRIGHT, *Circuit Judges,* join:

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* Circuit Judge Wilbur K. Miller became Senior Circuit Judge on October 16, 1964, and Circuit Judge Bastian became Senior Circuit Judge on March 17, 1965.

Nos. 17,953 and 17,954

Transit, the petitioner, and the intervenor alike attack the Commission's finding that a return of 4.87 per cent on gross operating revenues is "just and reasonable." Transit's argument essentially is that the Commission's finding is unsupported by substantial evidence, and that, in any event, a 4.87 per cent return is inadequate as a matter of law. Except for the points we have already discussed, however, Transit does not challenge the figures on which the Commission based its order, nor its estimate of the revenues Transit will earn at the fares allowed. The petitioner and the intervenor claim that the Commission relied solely, and thus erroneously, on the operating ratio method, disregarding all other criteria of a reasonable return. Specifically, they contend that the Commission mistakenly ignored the source and cost of Transit's capital requirements, the return on its rate base,[56]

[56] The PUC on two occasions resorted to the rate base method to "test the reasonableness of the rate of return computed under the gross operating revenue method . . . ." *D.C. Transit Sys., Inc.*, 38 P.U.R.3d 19, 45 (1961); see *D.C. Transit Sys., Inc.*, 33 P.U.R.3d 137, 149 (1960). While such

and the return on equity investment. They further contend that the Commission improperly relied on an earlier order of the Public Utilities Commission fixing Transit's return at 4.92 per cent.[57] And they, too, claim that the Commission's order lacks support in its findings or the evidence before it.

We express no opinion regarding the adequacy or inadequacy of the return allowed by the Commission, for we think that its order in this respect does not admit of the kind of meaningful judicial review contemplated by the statute. It appears to us likely that the Commission too narrowly conceived the scope of its inquiry under the operating ratio method, although, on this record, we can say only that the path it actually followed cannot confidently be discerned. *Colorado Interstate Gas Co.* v. *Federal Power Comm'n,* 324 U.S. 581, 595 (1945). The Commission concluded that Sections 6(a)(3) and (4) of the Compact required it to "'prescribe just and reasonable fares' based on the operating ratio theory of rate making." By virtue of Congress' mandate, therefore, it thought it was "not permitted to give significant consideration to return on equity," nor obligated to give more than "little consideration to return on [Transit's] . . . rate base." The Commission did concede that it was obligated to strike a balance between the interests of the company's stockholders

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an exercise may sometimes be useful, it surely is not essential, and the result reached can never be conclusive. The important thing is not that the result reached by the operating ratio method be compared with that which would have been reached under some other method, but that the operating ratio method be applied rationally and intelligibly in the first instance.

[57] This objection to the Commission's use of the earlier order reflects a misunderstanding of its opinion. We think that the Commission, essentially, was simply pointing out a mathematical coincidence, namely, that the new fares would produce approximately the same rate of return as the old.

and those of the riders by assuring sufficient revenues to cover expenses and capital costs while at the same time giving weight to the need for adequate, low-cost service. But it nevertheless insisted that,

> in determining reasonable earnings under the aforementioned guide lines . . . primary consideration must be given to the operating ratio theory and . . . *only minor consideration need be given the other factors brought into issue.*[58]

We do not quarrel with the Commission's conclusion that Congress intended that the operating ratio method should be the primary test of the reasonableness of Transit's fares. But the language that appears in its order strongly suggests that it misunderstood what that test entails. In *Federal Power Comm'n* v. *Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944), the Supreme Court enunciated what is now a fundamental principle of rate regulation: "Under the statutory standard of 'just and reasonable' *it is the result reached not the method employed which is controlling.*" (Emphasis added.) The Court went on to point out that, in balancing investor and consumer interests, it is essential to consider the capital costs of the enterprise. 320 U.S. at 603. Here, unlike the *Hope* case, Congress has specified what method of rate making the Commission should employ, but in so doing it did not relieve the Commission of the necessity of making the kind of inquiry that must be made if the statutory standard is to be complied with. A "just and reasonable" rate is one that assures that all the enterprise's legitimate expenses will be met, and that enables it to cover interest on its debt, pay dividends sufficient to continue to attract investors, and retain a sufficient surplus to permit it to finance down payments on new equipment and generally to provide

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[58] Order No. 245 (application of D.C. Transit System, Inc.), Washington Metropolitan Area Transit Commission, p. 44.

both the form and substance of financial strength and stability. A rate fixed without particularized reference to these needs does not satisfy any standard of rate making of which we are aware, including that of return on operating expenses. The operating ratio method does not make such an inquiry irrelevant; indeed, it was in part the failure of rates established by the rate base method to cover the capital costs of most motor carriers that led to its adoption.[59] An enterprise's operating ratio—the arithmetical ratio of its expenses to its gross revenues—may *suggest* that its rates are too high or too low, but whether they are too high or too low in fact depends in the final analysis on the degree of their correspondence to the items mentioned above. Rates that will produce an operating ratio of 95.13, therefore, do not possess some inherent validity, and whether they are proper in a given case requires a more detailed inquiry than the Commission here seems to have made.

We know from this figure of 95.13 only that the legitimate operating expenses found by the Commission—and we accept that legitimacy in this case—account for all but 4.87 per cent of the total revenues expected to be realized from the approved fare structure. We need to know more than we have been told about why the Commission thought this was the appropriate margin. The fixing of that margin is not in truth a process so greatly different from what is done in determining rate of return in traditional rate-base rate-making. There also the gross revenues allowed are to cover legitimate operating expenses in the first instance—and something more. That something more is the sum of money needed to attract the capital, both debt and equity, required to insure financial stability

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[59] See NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS, 64TH ANNUAL CONVENTION, *Report of the Special Committee to Study Principles of Rate Regulation in the Motor Bus Industry* 461, 468 (1953).

and the resulting capacity of the utility to render the service upon which the public depends. To determine that sum entails inquiries and findings—judgmental as the latter may often be because ratemakers must be prophets of the future as well as historians of the past—into such things as the capital programs in prospect, what such programs entail in terms of down-payments as well as financing, the cost of borrowing money, working capital needs, the desirable ratio of debt to equity, the incentives required by a stockholder to keep his money in the business and the dividends and growth rates requisite to supply these incentives, the opportunities in these respects provided in comparable businesses, and the related matters which must be prayerfully explored by the conscientious regulator before he can begin to say why he fixed upon 4.87 rather than 6.5 or 3.2.

A change from one rate-making method to another does not, we repeat, dispense with the necessity for this kind of inquiry. And any hopeful confidence we might have that such an inquiry may have been made but not articulated is scarcely enhanced by the Commission's statements to the effect that it did not regard it as either relevant or required under the operating ratio method—an error of which the Commission, as a new agency making its first start in the rate-making field, should be disabused at the outset in the interest of avoiding future difficulties. In any event, the Commission has described its deliberations and conclusions on this fundamental aspect of the case in terms of stock generalizations which serve only to frustrate, rather than illuminate, judicial review.

We are assured by the Commission that it considered Transit's "operating and financial needs . . . and all other relevant factors" in arriving at a return of 4.87 per cent. It says that it found that the new fares would "produce reasonable net revenues to allow [Transit] . . . to service its debt, pay reasonable dividends, retain a reasonable portion

in its business and to attract investments of private investors." But what facts it relied on the Commission does not say. It had before it a statement of Transit's current annual interest charges, but it seems to have made no inquiry into the cost to Transit of borrowing money, nor to have considered what Transit's future requirements in this regard are likely to be. Transit's annual dividend pay-out of about $500,000 appears to have been treated as if it were a cost of operation, like the annual expenditure for gas and oil, with no examination of, or conclusion about, its appropriateness. There is no suggestion in the Commission's opinion that it examined earnings on investments carrying comparable risks, or took into account Transit's peculiar capitalization. The Commission does not mention, if it considered, Transit's future equipment needs, if any, and how, or on what terms, such equipment could be financed. In short, we are left with only its assurance that it did in fact consider Transit's financial needs "and all other relevant factors." We do not know nor can we divine from the record what those needs are, much less what the Commission found them to be. Under these circumstances, our review can be no more than a "perfunctory process." *Colorado Interstate Gas Co.* v. *Federal Power Comm'n,* 324 U.S. 581, 605 (1945).

Transit began its life with a capitalization in which debt was heavily, and indeed strikingly, preponderant. As noted hereinabove, this was known to Congress when it passed the Franchise Act and directed that the rates then in effect be continued. This made inevitable large returns on equity to the extent that the relatively heavy interest requirements were safely covered and the gamble on traffic levels after the resumption of operations was won. The urgency of the problem of traffic uncertainty has, however, receded appreciably into the past. Although it continues to exist to some degree by reason of the seemingly

inexhaustible enthusiasm of motorists and highway builders, on the one hand, and persistent speculation about rail rapid transit, on the other, we think the time has come for the Commission to make a careful review and analysis of the earnings experience of Transit from its inception, and of what that experience has meant to the equity owners, both by way of dividend payments and growth in book values through retained earnings. We do not see how current fare increases can properly be appraised apart from such a study, and the reflection of its results in the articulation of the Commission's decision as to the margin of revenues over expenses appropriate to today's needs, as distinct from the crisis conditions of nearly a decade ago. It seems clear that Congress, by reason of the unusual specifications contained in the Franchise Act, intended the returns to be generous, for the purpose of restoring the then shattered public transit system to some semblance of stability. But if a measure of stability has been achieved, then the present ability of Transit to attract the capital it needs on relatively favorable terms may well be superior to what it was in the earlier years of its life. At least we cannot know that this is not true, unless the Commission identifies the role thus far played by Transit's earnings in bringing about such a condition.

This matter of earnings is the more important in the light of Congress' direction to the Commission, in Section 6(a)(3) of the Compact, to give due consideration in setting fares "to the need, in the public interest, of adequate and efficient transportation service by such carriers at the lowest cost consistent with the furnishing of such service." The Commission is thus required to see to it that the farepayers pay no more than is necessary to ensure the continued adequacy of the company's service and provide a return to the shareholders that is reasonable under the circumstances. The Commission in its opinion recognized that, "in the final analysis, the matter of fixing just and

reasonable rates involves a balancing of the investor and the consumer interests"; and we do not doubt its purpose to find that balance. Our difficulty, as we have said, arises from the Commission's failure to provide us an adequate basis for knowing why it did what it did.

We thus have no intelligible basis for disposing of the competing claims before us that the return allowed by the Commission is, on the one hand, too high, and, on the other, too low. We remand the case to the Commission for further proceedings consistent herewith to determine the margin of return over and above operating expenses that Transit should be allowed.

It is so ordered.

WRIGHT, *Circuit Judge, concurring*: Whatever system of rate making is used in determining a proper bus fare, two basic questions must be answered: (1) How much money have the owners of D. C. Transit invested in the company, and (2) what has been and what is the return on that investment. Until the Commission answers these two questions in words of one syllable so the public, and the court, can understand, the suspicion of unconscionable profits at public expense will persist. The present bus fare is very close to the highest charged in the country. Until the public knows how much the owners of D. C. Transit are making, and have made, on their investment, the bus riders ought not to be required to pay more.

The Government states in its brief:

> "• • • From 1957 through the first eight months of 1962 (for which year the figures were annualized), the Company averaged a 60 percent return on average book equity per year, a figure far in excess of the 23 percent which the PUC found 'to be more than sufficient to compensate investors for the use of their

funds.' The return for the individual years are (P. 11):

"1957	84.3
1958	58.8
1959	141.1
1960	28.3
1961	29.1
1962 (8 months annualized)	16.5

"Of interest for comparative purposes is the return on book equity made by D. C. Transit's predecessor, Capital Transit Co. (P. 11):

"1952	4.4%
1953	4.3%
1954	3.0%"

In view of this statement by the Government, the Commission in its opinion on remand should set out, year by year, beginning with 1956, the amount of capital actually invested by the owners[1] of D. C. Transit, followed by the earnings, year by year, on that investment. Thus the court, and the public, will know whether the owners of D. C. Transit have been, and will be, fairly compensated for their investment.

I am not suggesting that the line of inquiries indicated by the court is not necessary in determining a proper bus fare. Of course, it is. I am saying that the primary inquiry is: How much are the owners of D. C. Transit really making on the money actually invested in the company. The public is entitled to the answer to this question—in plain English.

WILBUR K. MILLER, *Senior Circuit Judge*, dissents.

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[1] Of course, if any capital has been returned to the owners, in any way, the year and amount thereof also should be disclosed.